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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 55

PACIFIC GAS AND ELECTRIC COMPANY, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION

OPINIONS BELOW

The decision of the Circuit Court of Appeals for the Ninth Circuit affirming the order of the Commission by an equally divided court (R. V, 1741), and the dissenting opinion of Judge Garrecht (in which Judge Mathews joined) (R. V, 1741), are reported in 139 F. (2d) 298.[1] The

[1] An earlier opinion in which the circuit court of appeals, by a majority of the three judges then sitting, affirmed the order of the Commission (R. V, 1699), is reported in 127 F. (2d) 378. After this first opinion a petition for rehearing was granted and the case was reargued before all seven judges of the court, sitting *en banc*. Judge Haney, who had written

opinion and order of the Commission (R. VI, 1883), dated September 10, 1941, are not yet reported.

JURISDICTION

The decree of the circuit court of appeals was entered on November 18, 1943 (R. V, 1776). A petition for rehearing was denied on February 23, 1944 (R. V, 1777). The petition for a writ of certiorari was granted on May 22, 1944. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, made applicable by Section 24 (a) of the Public Utility Holding Company Act of 1935.

QUESTIONS PRESENTED

1. Was there warrant in the record and a reasonable basis in law for the determination of the Securities and Exchange Commission that petitioner had not shown that its management and policies were "not subject to a controlling influence" by The North American Company within the meaning of Section 2 (a) (8) of the Public Utility Holding Company Act of 1935?

2. Did the court below err in entering a decree affirming the Commission's order when less than

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the earlier opinion on behalf of the majority, died between the second argument and the decision, with the result that the final decision was by an equally divided court of six judges. Only two of the three dissenting judges joined in the dissenting opinion.

a majority of the judges participating concurred in such action?

STATUTE INVOLVED

Section 2 (a) (8) of the Public Utility Holding Company Act of 1935 (49 Stat. 803, 807, 15 U. S. C. 79b (a) (8)) reads, in pertinent part, as follows:

> Sec. 2. (a) When used in this title, unless the context otherwise requires—
>
> * * * * *
>
> (8) "Subsidiary company" of a specified holding company means—
>
> (A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company (or by a company that is a subsidiary company of such holding company by virtue of this clause or clause (B)), unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; * * *
>
> The Commission, upon application, shall by order declare that a company is not a subsidiary company of a specified holding company under clause (A) if the Commission finds that (i) the applicant is not controlled, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) either through

one or more intermediary persons or by any means or device whatsoever, (ii) the applicant is not an intermediary company through which such control of another company is exercised, and (iii) the management or policies of the applicant are not subject to a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed in this title upon subsidiary companies of holding companies. The filing of an application hereunder in good faith shall exempt the applicant from any obligation, duty, or liability imposed in this title upon the applicant as a subsidiary company of such specified holding company until the Commission has acted upon such application. Within a reasonable time after the receipt of any application hereunder, the Commission shall enter an order granting, or, after notice and opportunity for hearing, denying or otherwise disposing of, such application. * * *

STATEMENT

1. *Summary of the Proceedings*

The petitioner, Pacific Gas and Electric Company (hereinafter referred to as P. G. & E.), filed

an application under Section 2 (a) (8) of the Public Utility Holding Company Act of 1935 (hereinafter referred to as the Act) for an order declaring it not to be a subsidiary of The North American Company (hereinafter referred to as North American). The application was denied (R. VI, 1883 *et seq.*).

P. G. & E. is predominantly an electric and gas public utility operating company (R. I, 45–100).[2] As of the date of its application for an order declaring it not to be a subsidiary of North American, the latter company owned, controlled and held with power to vote 32.89% of petitioner's common stock, constituting 17.71% of P. G. & E.'s outstanding voting securities (R. I, 75).[3]

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[2] Petitioner is also a holding company, but has been exempted from regulation as such under the Act by reason of its intrastate character. Concurrently with the filing of its application for an order declaring it was not a subsidiary of North American, petitioner filed an application pursuant to Section 3 (a) (1) and (2) of the Act for an exemption as a holding company with respect to its ownership of 45.8% of the voting securities of Vallejo Electric Light and Power Company, an electric utility company operating in Vallejo, California (R. I, 2–100). This application was granted by the Commission (R. VI, 1932), and no question with respect thereto is raised in the present proceedings.

[3] Since the date of the Commission's order, North American has distributed some of petitioner's common stock as dividends. As of October 2, 1944, its holdings had been reduced to 24.99% of the common stock, comprising 13.02% of petitioner's voting securities. North American has committed itself to a program of systematic disposition of its P. G. & E. stock under which it will reduce its holdings below 10% by January, 1946, if dispositions are continued at the present

Since more than 10% of P. G. & E.'s outstanding voting securities are owned by North American, petitioner is a "subsidiary company" of North American under Section 2 (a) (8) (A) of the Act, unless, under the second paragraph of that section, the Commission should enter an order declaring it not to be such a subsidiary. P. G. & E.'s application for such an order alleged and offered to establish that (1) it is not controlled, directly or indirectly, by North American; (2) it is not an intermediary company through which control of another company is exercised; and (3) its management or policies are not subject to a controlling influence, directly or indirectly, by North American, so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that it be subject to the obligations, duties and liabilities imposed in the Act upon subsidiary companies (R. I, 2–100).

On September 4, 1940, the Commission issued its notice of and order for hearing with respect to petitioner's application (R. I, 101). Hearings were held before a trial examiner in San Francisco and New York. At the request of petitioner, the Commission directed the Trial Examiner to file a Report and Findings of Fact. The Report and

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rate. It is also under order to dispose of that stock and it has urged no error in that determination except the general constitutional objection raised in the proceeding now pending on the special calendar of this Court, *North American Co.* v. *Securities and Exchange Commission*, No. 1, present Term.

Findings of Fact filed by the Trial Examiner (R. VI, 1779–1882) concluded that petitioner was entitled to the order which it sought, and counsel for the Commission filed exceptions. Briefs were filed and the matter was argued orally before the Commission. On September 10, 1941, the Commission issued its findings and opinion (R. VI, 1883–1931) and entered its order (R. VI, 1932–1933) denying petitioner's application to be declared not to be a subsidiary of North American because it was unable to make the finding required by clause (iii) of Section 2 (a) (8), i. e., that petitioner's management and policies "are not subject to a controlling influence" by North American "so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers" that petitioner be subject to the Act.[4]

Upon a petition for review, the circuit court of appeals affirmed the Commission's order, at first by a two to one decision (R. V, 1699–1738), and then, upon reargument before the court *en banc* (R. V, 1739–1740), by an equally divided court (R. V, 1741).[5]

[4] The Commission deemed it unnecessary to consider the questions raised under clauses (i) and (ii) of Section 2 (a) (8), since the petitioner did not meet the conditions of clause (iii) and compliance with the statutory conditions contained in all three clauses is a prerequisite to exemption under the Section.

[5] Section 2 (a) (8) grants a temporary exemption, based upon the filing of an application in good faith, "until the

2. *The facts*

The facts, as detailed in the findings and opinion of the Commission (R. VI, 1883–1931), may be summarized as follows:[6]

P. G. & E. is a California corporation, organized in 1905, and primarily engaged in the production, purchase, transmission, distribution and sale of electric energy and natural and manu-

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Commission has acted upon such application." Notwithstanding the fact that the Commission acted upon its application on September 10, 1941, the petitioner has not subjected itself to regulation under the Act, relying upon an *ex parte* "stay" granted by the circuit court of appeals on September 19, 1941, and continued by orders dated February 23 and October 9, 1944, pending the outcome of the case in this Court (R. V, 1696, 1777, 1936). The Commission's motion to vacate the "stay" was not passed on by the court in either of its decisions, the stated ground in the first decision being that it had become moot (R. V, 1703–1704).

[6] The petitioner, at pages 10–21 of its brief, attempts to summarize the findings of the trial examiner, stating that "these findings may be considered as an undisputed statement of the facts of the case." In its opinion (R. VI, 1912), the Commission had stated: "There is *almost* no dispute *as to the facts* in the case as they are set forth in the trial examiner's report and in the briefs of both counsel." [Emphasis supplied.] Although it is true that there was no dispute as to the evidentiary facts, certain inferences and conclusions based thereon made by the trial examiner and set forth in his findings, which the petitioner has undertaken to summarize, have not been accepted or adopted by the Commission. The Commission reviewed the detailed facts in the record and drew its own inferences and conclusions. Accordingly, the trial examiner's "findings" may not be considered as an undisputed statement of the facts of the case. Our counterstatement of the facts is set forth in the text.

factured gas in northern and central California. Since 1905, it has acquired, by direct purchase or by exchange of stock, the properties of over 400 separate companies, and it is today one of the largest public utility companies in the United States. (R. I, 3, 127–140.) It supplies electricity to approximately 909,155 customers residing in 372 California communities, and supplies gas at retail to about 636,316 customers in more than 180 California communities. P. G. & E.'s total assets, as of June 30, 1940, were stated on its books at $791,146,218 (Pet. Ex. 36f). Its gross operating revenues for 1939 amounted to $107,-175,353 (R. I, 94).

North American, a New York corporation, is exclusively a holding company registered as such under the Act. It does not operate any utility properties, but has operating subsidiaries in several states. It is by far the largest stockholder of P. G. & E. As of August 1, 1940, North American owned, controlled or held with power to vote 2,059,670 of petitioner's 6,261,273 shares of outstanding common stock (R. I, 74, 75). This represented 32.89% of petitioner's outstanding common stock and was carried on North American's books at over $63,000,000. The dividends from it have constituted between 20% and 25% of North American's corporate gross income. (R. IV, 1545–6.) As of the same date, P. G. & E. also had outstanding 5,370,822 shares of preferred

stock, none of which was owned by North American (R. I, 74). This stock has equal voting rights with the common, so that North American's common stock holdings constituted 17.71% of petitioner's total outstanding voting stock (R. I, 75).

The next largest stockholder, Standard Gas and Electric Company, owned, as of the same date, 200,420 shares of petitioner's common stock or 1.72% of its voting securities (R. I, 75).[7] Generally speaking, the remainder of P. G. & E.'s voting securities are widely scattered among its 95,891 stockholders (Pet. Ex. 20 and 29).

North American's interest in P. G. & E. dates back to 1930. At that time North American had a subsidiary holding company, Western Power Corporation, with three public utility subsidiaries operating in California. One of these subsidiaries, Great Western Power Company of California, had been the principal competitor of petitioner and derived 90% of its operating revenue from territory also served by petitioner. In June, 1930, P. G. & E. issued 1,825,000 shares of its common stock in exchange for Western Power Corporation's holdings of securities in its California public utility subsidiaries and the cancellation of

[7] Other large stockholders are The Sun Life Assurance Company of Canada, which owns 120,198 shares of common stock and 55,000 shares of preferred stock; Pacific Lighting Corporation, a California corporation, which owns 131,900 shares of common stock; and the American Superpower Corporation, a Delaware corporation, which owns 100,000 shares of common stock (Pet. Ex. 20 and 21).

certain indebtedness owed by these subsidiaries to Western Power Corporation (Pet. Ex. 6; R. III, 1051–3). James B. Black, later to become president of P. G. & E., was the principal representative of North American in the negotiations with P. G. & E. which led to its acquisition of North American's California subsidiaries. Black had been vice president, general manager and a director of Great Western from 1922 until 1927, at which time he went to New York as vice president of North American, with the principal duty of keeping in touch with and assisting the three California subsidiaries. Close contact was maintained between the local operating men and Black. (R. III, 1046–1053; VI, 1892–3.)

In 1936 Western Power Corporation was dissolved, and its holdings of P. G. & E. common (including 252,055 additional shares which had been purchased in 1931 by the exercise of preemptive rights and the acquisition of which had therefore not increased Western's—and North American's—proportionate interest in P. G. & E.) were transferred to North American (Comm. Ex. 56, 57 and 58).

At the time of the negotiations with North American petitioner's directors were apprehensive of the power that North American would acquire by the ownership of such a large block of securities. Hockenbeamer, then president of P. G. & E., told the directors that North Ameri-

can had given him assurance that it would not "dominate" or interfere with P. G. & E.'s management.[8] Black testified that he assured Hock-

[8] Thus, Allen L. Chickering, one of the petitioner's directors, testified (R. II, 735, 778–779):

Q. Now, during those discussions and before the transaction was authorized by the Board of Directors, were there any discussions with respect to the position of the North American Company as a stockholder after the transaction was consummated?

A. Yes sir. The first thing that I objected to was the North American domination. I said I was afraid of it and Mr. Hockenbeamer said that he had been assured that there would be no domination, that they simply have an investment position; they wanted to have three members on the Board of Directors but that they would not exercise any domination or attempt to increase their holdings. Now, I only know that from Mr. Hockenbeamer. I didn't talk with Mr. Black myself.

Q. That statement was made by Mr. Hockenbeamer?

A. Yes sir.

Q. Before the transaction was consummated?

A. To the Executive Committee?

Q. Yes.

A. It was one of the first points the committee brought up, the objection of that sort.

* * * * *

Q. What discussion was had in 1929 and 1930 concerning the extent to which it was contemplated that North American might participate in the Applicant's affairs if it acquired a large block of its common stock?

A. Well, naturally all we knew was that Mr. Hockenbeamer told us and I for one, and several other directors, were apprehensive of any holding company acquiring such a large interest and we voiced that apprehension in the meetings of the Executive Committee. Mr. Hockenbeamer told us that the North American Company would take an investment interest only and would not

enbeamer that, in so far as he could direct the policy, there would be no interference by North American. However, with respect to this general understanding, Black stated that "There was nothing ever said about how long it should last or any considerations as to changes if conditions changed in the future" (R. III, 1060–1). Apparently an attempt had been made by P. G. & E. to secure an irrevocable proxy from North American, but North American seems to have been unwilling to go so far in committing itself to non-interference.[9]

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make any effort to control us. He also told us that they would not increase their proportionate ownership in our stock. Whether there was any agreement to that effect or not, I don't know, but we took Mr. Hockenbeamer's word for it.

Q. Would you say that those assurances by North American were received at the insistence of certain members of the Applicant's Board?

A. Well, I think that all of us felt that way, Miss Calkin. I think even Mr. Hockenbeamer felt that way.

[9] Mr. Hockenbeamer, president of P. G. & E., sent a cable to C. O. G. Miller, one of the petitioner's directors, then on a world cruise, reading in part: "Three directors one member executive committee no proxy but positive assurances non interference" (Pet. Ex. 43A). In connection with this cable and the apparently unsuccessful attempt to secure an irrevocable proxy, Miller testified (R. II, 620–621):

Q. Referring to Applicant's Exhibit 43 (a), I believe, which is the telegram you received from Mr. Hockenbeamer, wherein it is stated that, in substance, the North American Company would not give a proxy, what was your understanding of that language in that telegram?

A. The meaning of the telegram?

Q. Yes—that portion of it.

The agreement between North American and P. G. & E. was never formalized, nor was any time limit placed on North American's assurances of non-interference (R. I, 226–7, 257–9; II, 735–6, 778–9, 831–2; III, 1059–1062, 1123, 1127–1130).

It was orally agreed, at the time of the 1930 transaction, that North American would be entitled to name three directors of P. G. & E.'s Board of fifteen [10] and one member of its Executive Committee (consisting of four directors and the president of the company) (R. III, 1059–1062, 1123).

Pursuant to this oral agreement, Black, then a vice president of North American, Guy C. Earl, a former president of Great Western Power Company of California, and Edwin Gruhl, then vice president and general manager of North American, were elected to P. G. & E.'s Board on June 18, 1930. Black was also appointed to the Executive Committee but was replaced in a few weeks by Earl. (Pet. Ex. 16 and 17.)

A. That the North American Company would not give an irrevocable proxy, but had promised in good faith not to attempt to obtain control or seek proxies.

Q. It means it would not give any irrevocable proxy for the slate of the directors that the management might choose?

A. I would put it broader than that: That they were unwilling to give an irrevocable proxy to anyone for a long period of years. It was not unexpected by me, at least.

[10] This was the minimum number of directors which North American would be able to elect by cumulating and voting its shares (R. VI, 1823).

Earl served continuously and very actively as a director and member of the Executive Committee until his death in June, 1935. During this period he attended substantially all of the meetings of these two bodies, and took copious notes of what transpired, which he sent to Black together with copies of the minutes of the meetings of the Executive Committee and various reports which were furnished to directors and Executive Committee members. (Pet. Ex. 19; R. I, 276; III, 1154–1155.) For these services, North American paid Earl $12,000 a year (R. III, 1440); he received no salary from P. G. & E.

During this period one of Black's principal duties as an employee of North American was the maintenance of careful scrutiny over the affairs of P. G. & E., and although he attended only four meetings of petitioner's Board, he was able to watch over petitioner's affairs through Earl's detailed reports and by fairly extensive correspondence with Hockenbeamer. The latter sent numerous reports and financial statements along with his letters, which often gave detailed explanations of P. G. & E.'s operations. (R. III, 1180–3; VI, 1900–1.)

Petitioner's president has always been its chief executive officer (R. VI, 1902). Upon Hockenbeamer's death in 1935, the Executive Committee, which then consisted of three San Francisco business men, decided to recommend to the Board of

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Directors Black's election as president (R. II, 611–612, 633–635). After several conferences with local non-employee directors, C. O. G. Miller, one of the Executive Committee members, called Fogarty, president of North American, and obtained permission to offer the position to Black (R. II, 613–615, 633). Miller then called Black, who agreed to accept the presidency if elected (R. II, 634–635). At the insistence of another director, Miller called Black a second time and asked him whether, if elected president, Black would sever all his relations with North American. Black replied in the affirmative. Shortly thereafter, Black was elected to the presidency. This was in November, 1935, when the Holding Company Act was about to go into effect. (R. II, 611–616, 633–635, 738–742; III, 1442–1445.) Since then, North American has not named a representative on petitioner's Board of Directors to replace Black, nor has it named a representative to the Executive Committee in Earl's place. Thus, since the date of Earl's death and the appointment of Black as president of P. G. & E., North American has had only two directors and has had no representative on the Executive Committee. North American's two other representatives on the Board have attended practically no meetings and no one was ever selected to perform the duties performed by Earl. (R. III, 1155; IV, 1473; Pet. Ex. 16 and 18.) And no one in New York has replaced Black, whose principal

function was to follow P. G. & E.'s affairs closely for North American (R. III, 1155–6; IV, 1473–4).

North American's present representatives on P. G. & E.'s Board are J. F. Fogarty, formerly president of North American and now chairman of its executive and finance committees, and H. C. Freeman, vice president of North American (R. VI, 1901; Pet. Ex. 16).

None of P. G. & E.'s other large stockholders is represented on its Board.[11]

P. G. & E. regularly sends to North American a variety of detailed weekly and monthly reports. After Earl's death, Hockenbeamer instructed Foote, petitioner's secretary, to send North American the same reports and documents Earl had sent (R. II, 496); and, as already stated, Hockenbeamer himself sent numerous reports, frequently accompanied by detailed letters of explanation, to Black, then North American's vice president, in New York (R. III, 1180–1184; VI, 1900–1, 1907–8; Comm. Ex. 72–105).

Fogarty and Freeman, as North American's representatives on P. G. & E.'s Board of Directors, regularly receive the minutes of direc-

[11] The Commission noted the possibility that C. O. G. Miller, chairman of the Board of Pacific Lighting Corporation, which owns 131,900 shares of P. G. & E.'s common stock, might be considered a representative of that company, but indicated that he was not generally so regarded (R. VI, 1901). In any event it is clear that Miller was not a representative of Pacific Lighting Corporation in the sense that Fogarty and Freeman are representatives of North American.

tors' meetings and certain other data sent to all directors.[12] In addition, however, even though they are not members of P. G. & E.'s Executive Committee, they receive the minutes of the weekly meetings of that Committee and all reports and statements regularly made available only to members of that Committee. These are sent to them either weekly or monthly.[13] Furthermore, P. G.

[12] These include (Pet. Ex. 33)—

(1) Consolidated income statements in comparative form—month, year to date, and 12 months to date—with supplementary statements showing revenue and expenses by major departments, accounting classifications, and geographical divisions; (2) Consolidated balance sheets in comparative form, with supporting schedules showing outstanding stocks and bonds, together with income statements and supplementary statistical data.

[13] Fogarty and Freeman receive each week (Pet. Ex. 33; R. VI, 1908)—

(1) Cash reports showing collections and disbursements;

(2) Expenditures authorized under general manager estimates submitted to the executive committee for approval;

(3) System generating report showing power output, system peaks and precipitation data;

(4) Consolidating operating report of the Natural Gas Division of gas received and gas sent out;

(5) Statement of new business connected, electric and gas;

(6) Minutes of meetings of the Executive Committee.

Monthly they also receive the following (Pet. Ex. 33; R. VI, 1908)—

(7) Customers' statement showing gain or loss in customers by departments and divisions;

(8) Capital expenditures statement showing gross capital expenditures and property retired, work in progress, general manager estimates transferred to plant account, capital expenditures covered by division managers' authorization, and status of purchasing department contracts.

& E. also regularly sends to Fogarty and Freeman, as North American's representatives, the following reports and data which are not furnished either to its directors or Executive Committee members (R. I, 419–428; II, 495–9, 523, 747–750; VI, 1909; Pet. Ex. 33 and 45):

(1) Copies of gas and electric rate schedules, revised from time to time by the filing of new schedules with the California Railroad Commission;

(2) Copy of report submitted to the Edison Electric Institute, showing sources and disposition of electric energy and classifications of customers;

(3) Copies of "Report for Insurance Companies" prepared annually and sent to large insurance companies and other institutional investors;

(4) Statistical statements prepared by the Department of Vice President and Executive Engineer;

(5) Rate schedules filed with the California Railroad Commission;

(6) Court decisions and orders of the Railroad Commission of interest to P. G. & E.

North American has never requested any information from P. G. & E. which has not been furnished (R. IV, 1609).

Black and Fogarty have called each other by telephone from four to nine times each year since

Black became president. Their conversations were with regard to the bond market, settlement of a rate case, and contemplated refundings (R. III, 1162–1163, 1446). Black has been in New York twice and Fogarty in San Francisco four times since 1935. On each of these occasions Fogarty and Black discussed petitioner's affairs in a general way (R. III, 1080; IV, 1484–1487). In connection with public financing by P. G. & E. in 1936, Black talked to Fogarty on the telephone to obtain his opinion on the bond market (R. III, 1273–1274; IV, 1537). He also sought Fogarty's advice as to discounts in connection with a later sale of a $15,000,000 bond issue to institutional investors (R. III, 1289). This practice of asking North American's advice in connection with proposed financing had also been followed by Hockenbeamer in telephone conversations with Black when the latter was vice president of North American (R. III, 1066–7, 1263–5; VI, 1905–6).

North American has never performed any services for P. G. & E. and, except for the receipt of dividends, has never engaged in any monetary transactions with P. G. & E. (R. I, 228; II, 525, 545; III, 1083; IV, 1582).

The record shows only one occasion, prior to the time when Black became president, when North American's wishes on a particular matter were

contrary to the action of P. G. & E.'s directors. In 1933, petitioner's directors reduced the quarterly dividend on the common stock from 50 cents per share to 37½ cents per share because of a decreased trend in earnings. North American's president called Hockenbeamer and urged him to have the matter reconsidered, if possible (R. III, 1068–9). Black sent a telegram asking reconsideration (R. II, 670; III, 1067–9). Although the matter was not reconsidered (R. III, 1069), the record does not reveal that any further attempt was made to obtain reconsideration (R. III, 1209).[14] However, in the fall of 1936, Black, who had by then become president of P. G. & E., recommended the restoration of the 50 cents per share dividend and the Board restored the larger dividend. Black testified that the earnings justified the restoration, and that North American had not requested the action. (R. III, 1209–1210; II, 639–641, 870–1; VI, 1911.)

P. G. & E.'s proxy committee for many years has consisted of its president, vice president and general manager, and the secretary and treasurer (R. III, 1088–9). It has been customary for the proxy committee to seek the election of the incumbent directors, including the North American representatives (R. II, 693–4; III, 1144–5).

[14] See note 32, *infra*.

When Black was with North American, he usually wrote Hockenbeamer each year requesting that the current North American representatives be reelected (Comm. Ex. 59, 62, 67, 68). More recently no such requests have been made, but petitioner's proxy committee has nevertheless included the incumbent North American representatives in its proxy, on the assumption that North American would communicate any desire to have the personnel of its representation changed (R. III, 1145, 1469–1470). North American has always forwarded its proxy to the management's proxy committee (R. IV, 1581–2).

Under the corporation laws of California, the presence in person or by proxy of the holders of the majority of the shares entitled to vote in any stockholders' meeting constitutes a quorum for the transaction of business, and if a quorum is not present a majority of the shares in attendance may adjourn the meeting, but no other business may be transacted (R. VI, 1898) (Deering's Civil Code of California (1937), Section 316). Since 1932 (until April 9, 1940) at no meeting were enough shares present, apart from the shares held by North American, to constitute a quorum (R. VI, 1898–9). North American's holdings have represented from 27% to 30% of the total votes

cast at each of the stockholders' meetings held during that period (Pet. Ex. 23, 26).[15]

Apart from evidence regarding the specific matters described above, the record contains testimony, not disputed by the Commission, that P. G. & E.'s local directors are men of substance, with a keen sense of local pride in their community and in their company as a community enterprise.[16] The record further contains uniform protestations, by officials of both P. G. & E. and North American, as to the absence of control or controlling influence. Testimony to this effect,

[15] See the following table (R. VI, 1899):

Date of meeting	Percentage of shares represented in person or by proxy	Percentage of total votes cast by North American	Approximate percentage of voting securities owned by North American at date of meeting	Percentage of total outstanding shares present exclusive of North American
Apr. 12, 1932	67.5		19.2	48.3
Apr. 11, 1933	66.5		18.1	48.4
Apr. 10, 1934	61.0	28.5	18.0	43.0
Apr. 9, 1935	58.3	30.5	18.1	40.2
Apr. 14, 1936	64.1	27.9	18.0	46.1
Apr. 13, 1937	64.3	27.8	17.9	44.4
Apr. 12, 1938	64.5	27.8	17.9	44.6
Apr. 11, 1939	64.9	27.3	17.7	47.2
Apr. 9, 1940	62.6	28.3	17.7	44.9

No record of individual proxies was kept in 1932 and 1933.

[16] In this connection it should be noted that as of August 1, 1940, more than half—52.1% of P. G. & E.'s voting stock—was held by stockholders resident outside the state of California.

which the petitioner regards as "uncontradicted evidence" of compelling weight (see Br., p. 95), is in our judgment more properly to be regarded as constituting the mere argumentative conclusions of the witnesses as to the ultimate issue in the case. As against such testimony, it is clear from the record that, with the exception of the dividend reduction episode mentioned above, North American has always supported P. G. & E.'s management, and has done so as a deliberate business policy fashioned in its own interest. Freeman testified: "It is a situation in which our interest in the company is best served by that company being regarded as a California company, under California management" (R. IV, 1642). And Fogarty testified that North American's present inactivity in the affairs of P. G. & E. is due primarily to the fact that P. G. & E.'s business has enjoyed a normal growth and has progressed in a satisfactory manner (R. IV, 1545–6). If conditions changed, so would North American's attitude, for, as Fogarty testified, "If some conditions were to develop which were the result of improper or incompetent management, it would be an entirely different situation," and he and Freeman would then "take a more active part in the directors' meeting than [they] had in the past" (R. IV, 1545–8).

On the basis of a record in which the foregoing evidentiary facts were not in dispute the Commis-

sion decided that P. G. & E. had not sustained the burden of proving that its management and policies were not subject to a controlling influence by North American so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that it be subject to the obligations imposed by the Act upon subsidiaries of holding companies. Accordingly, the Commission denied P. G. & E.'s application for an order declaring it not to be a subsidiary of North American.

If the Commission's order is affirmed and the petitioner is subjected to regulation as a subsidiary company of a holding company under the Act, the principal practical effect will be to require Commission scrutiny of petitioner's security issues and, possibly, to require that such issues be sold at competitive bidding. Regulation as a subsidiary will in addition subject petitioner to a variety of restrictions such as those prohibiting a holding company subsidiary from having on its Board of Directors investment bankers, or commercial bankers from areas outside that in which the company operates. The petitioner contends—and, except as to the requirement of competitive bidding for security issues, we concede—that its policies in the past have not been inconsistent with the restrictions which have been imposed upon subsidiaries under the Act. Subjection of

the petitioner to these restrictions will, however, serve the purposes of the Act in protecting against possible future changes in the petitioner's policies so long as it remains subject to a controlling influence by North American.[17]

SUMMARY OF ARGUMENT

1. The petitioner, in an attempt to pitch the controversy in the field of statutory construction, ascribes to the Commission various interpretations of the Act which it asserts misled the Commission into erroneous application of the standards of Section 2 (a) (8). Thus, the petitioner claims, among other things, that the Commission has construed the phrase "'subject to a controlling influence" as if it referred merely to "influence", whether or not controlling, and has treated it as comprising merely the possibility of "purely hypothetical future machinations". The Commission

[17] See discussion at pp. 70–73, *infra*. Since the Commission's opinion in this case, the Commission has in other proceedings ordered North American to dispose of its holdings of petitioner's stock, and North American has already entered upon a program of disposition which will probably result in bringing its holdings below the statutory 10% within approximately the next year. See note 3, *supra*. Thus, the decision of this case, if favorable to the Commission, will subject the petitioner to the responsibilities and restrictions of a subsidiary for only a relatively short period. However, the validity of the Commission's order is of course to be considered in the light of conditions as they existed when the order was made, at which time there was no basis for forecasting how long petitioner was likely to remain in the status of a subsidiary.

has taken no such position. It has followed its view, consistently applied in its previous decisions in comparable cases and consistently upheld by the courts on review, that the "controlling influence" contemplated by the Act may include latent, unexerised power to exert controlling influence. The petitioner does not now dispute this proposition; and from it must follow the conclusion that a showing of the absence of either past or present active interference in management or policies is not necessarily sufficient to carry the burden of proof that the holding company possesses no latent power to exert a controlling influence. Congress contemplated that the term "controlling influence" should be construed with sufficient flexibility "to meet the varied and subtle forms which corporate interrelationships have in the past and will in the future take". The petitioner's assertion that the Commission has applied an erroneous standard of "controlling influence" is in our judgment merely an argumentative statement of the petitioner's own conviction that as a matter of factual inference the Commission's ultimate conclusion, that petitioner had not established its right to relief, was without rational basis in the record.

The same is true of the Commission's asserted "errors of law" with respect to the burden of proof. There is no basis for claiming that the Commission's occasional use of the word "demonstrate," interchangeably with such practically

synonymous expressions as "show," "prove," "establish," and "meet," was intended to, or did, impose upon the petitioner an improper burden of proof. Nor did the Commission regard the substantial stockholdings of North American as creating an irrebuttable presumption of the existence of controlling influence; it weighed that fact, as evidence, as it did all other pertinent facts, giving consideration not only to the size of North American's holdings but also to the relative size and distribution of other holdings of petitioner's stock, and to the historical facts of North American's position and influence as a stockholder. Upon the whole record, the Commission concluded that the evidence was not sufficiently strong to establish that petitioner was not "subject to a controlling influence" by North American. The dispute as to the soundness of this conclusion involves no substantial issue of law, but merely an issue as to the propriety of the inferences which the Commission drew from the record.

2. The test of the propriety of the Commission's conclusion is not whether the Court would as a matter of first instance have drawn the same inferences from the record as did the Commission, nor even whether other, and conflicting, inferences might not equally well be accepted. It is, rather, merely whether the Commission's conclusion "has 'warrant in the record' and a reasonable basis in law". *National Labor Relations Board* v. *Hearst*

Publications, 322 U. S. 111, 131. The Commission's determination in this case did have "warrant in the record". Undisputed evidence showed that North American held nearly one-third of petitioner's common stock, amounting to 17.71% of its outstanding voting securities, all other stockholdings being relatively small and widely scattered. This investment represented a substantial part of North American's own portfolio, being carried on North American's books at $63,000,000, and the dividend income from it constituting from 20% to 25% of North American's entire corporate income. North American had maintained close scrutiny of petitioner's operations since the inception of their connection; it secured frequent and detailed reports, more extensive even than those received by the petitioner's own Board of Directors and Executive Committee. Petitioner's president since 1935 had been a man who prior thereto was a trusted executive of North American, charged primarily with supervising North American's interest in petitioner. At all stockholders' meetings since 1932 North American's proxy had been necessary to create a quorum; and its stockholdings had at all time been sufficient to give it a veto power over important organic forms of corporate action.

As against these facts, the petitioner urges an absence of evidence of active efforts on the part of North American to control or direct its manage-

ment or policies. The Commission was entitled, however, to conclude that the absence of any such evidence did not establish that North American was not in a position to exercise, and would not have exercised, such controlling influence if at any time it had been in its interest to do so. The record establishes that North American, through the close scrutiny which it maintained over petitioner's operations, was fully satisfied that those operations were being conducted to its advantage, and that no purpose would be served by its undertaking to exert its controlling influence to alter the present managerial policies. North American's representatives on petitioner's Board testified that it was good "public relations" to have petitioner "regarded as a California company, under California management," and that it would be undesirable for North American to intervene in the situation unless "some conditions were to develop which were the result of improper or incompetent management." The Commission's extensive contact with the problem of control relationships not only under the Public Utility Holding Company Act but under the other legislation which it administers gives it peculiar competence to detect and appreciate the subtle means by which controlling influence may be exerted. The question whether, assuming the existence of such a "controlling influence," regulation is necessary or appropriate in the public interest, is likewise one peculiarly for administrative deter-

mination. Here, the Commission determined that petitioner had not shown that its management and policies were not subject to a controlling influence by North American, and that it had also failed to establish that regulation was not necessary or appropriate in the public interest. These determinations, being within its administrative competence and warranted by the record, should be permitted to stand.

3. There is no substance to the petitioner's claim that because less than a majority of the court below concurred in the view that the order complained of should be affirmed, petitioner has been deprived of judicial review contemplated by the Act. The Commission's orders under Section 2 (a) (8) are self-operative, and not dependent upon judicial sanction for their effectiveness. If less than a majority of the reviewing court acts to set them aside, they must stand, as does any judicial order in similar circumstances. In any event, the entire case is now before this Court for decision on the merits, and this Court is in a position to furnish full judicial review. Remand to the circuit court of appeals for a third hearing would serve no purpose but that of delay.

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ARGUMENT

I

THERE IS NO SUBSTANTIAL DISPUTE BETWEEN THE PARTIES AS TO STATUTORY CONSTRUCTION

In view of the frequently expressed reluctance of this Court to disturb administrative findings and factual conclusions which have warrant in the record presented to the administrative body, it is not unnatural that petitioner strains to discover legal issues in controversy, and to impute to the Commission conclusions or assumptions of statutory construction which, if erroneous, might vitiate the Commission's ultimate conclusion that petitioner had not established its right to the relief it sought. These efforts, we believe, must fail. They rest primarily on overrefined analysis of selected phrases in the Commission's opinion, and on tenuous and imaginative inferences, from what the Commission did not say, as to what the Commission might have thought or meant. We believe that a full and fair reading of the Commission's opinion as a whole, and of the affirmative contentions of statutory construction advanced by the petitioner, will suffice to sweep away the asserted issues of law, and place the controversy on its proper basis, as a controversy as to the sufficiency of the record to support the Commission's ultimate factual conclusion.

Whatever may have been the petitioner's position at earlier stages of the case, petitioner does not now contend that the statutory standard may be met by showing merely that no "controlling influence" is being currently exercised. Petitioner concedes in its brief (p. 39) that, at least for the purpose of this argument, "we may assume that the present existence of the power, whether or not in the process of being exercised, is sufficient. That is to say—it may be sufficient if the power exists though quiescent."

That likewise is the Commission's position; and nothing in the Commission's opinion, or in its opinions in comparable cases involving the application of the same statutory standard, justifies the petitioner's assertions that the Commission has accepted "purely hypothetical future machinations" as equivalent to "controlling influence" (Pet. Br., p. 39), or has construed "controlling influence" as meaning "influence" only (Pet. Br., p. 46). Petitioner's assertions, presented as points of statutory construction, in reality amount to argumentative statements of petitioner's own view that the conceded facts could not rationally support the inferences drawn from them by the Commission. That the record does support the inferences drawn from it by the Commission is the subject of Point II of our argument; but before reaching that point, and rather than dispersing the argument over the dozen or so "legal"

issues which the petitioner seeks to inject into the case, we think it best to explain affirmatively what we regard as the proper statutory standard, as it has been construed and applied by the Commission and the courts in this and other comparable cases.

1. *The Meaning of "Controlling Influence"*

In this case, as in others, the Commission has declined to accept, as establishing lack of "controlling influence", a mere showing that the holding company has not actively interfered in the subsidiary's management in the past, or is not currently so interfering. This position must be sound if, as the petitioner now concedes, the existence of a latent, unexercised power to control or to exert a "controlling influence" is sufficient to defeat the claim to exemption; for it would be a *non sequitur* to permit a showing of non-exercise of a power to be determinative of its non-existence. In the language used by the Commission in this case (R. VI, 1913), "to prove an absence of control or controlling influence, the applicant must do more than show that the holding company has not actively interfered with the local management in the past, for, as we understand the language of Section 2 (a) (8), 'control' includes the power to control, and 'subject to a controlling influence' includes susceptibility to domination. Rochester Telephone Corporation *v.* United States, 307 U. S. 125 (1939); The Hartford Gas Company, 8 S. E. C. ____ (1941), Hold-

ing Company Act Release No. 2613; The Detroit Edison Company, 7 S. E. C. 968 (1940)."

This is no novel theory adopted for the purposes of this case, but one consistently applied by the Commission throughout its administration of the Act, and as consistently affirmed by the courts which have reviewed the Commission's orders. In *The Detroit Edison Company*, 7 S. E. C. 968, 969 (1940),[18] the first case under Section 2 (a) (8) to reach the courts, the Commission expressed the doctrine somewhat more fully:

> But whether the holding company has exercised control or effectively exerted influence is, upon application such as this, material only insofar as such circumstances may evidence the existence in the holding company of the ultimate directory power. Inaction on the part of a holding company does not necessarily negate the existence of control or controlling influences. It may only evidence satisfaction with the manner in which a subsidiary is being operated. A subsidiary company, moreover, does not cease to be such merely because it has been given the opportunity to build up an able and self-contained management. The problem is one of fundamentals and not superficialities for, as we understand the statutory language, "control" embraces the power to control and "subject to a controlling in-

[18] Affirmed, *Detroit Edison Co.* v. *Securities and Exchange Commission*, 119 F. (2d) 730 (C. C. A. 6), certiorari denied, 314 U. S. 618.

fluence" includes susceptibility to domination (*Rochester Telephone Corporation* v. *United States, supra*). Consequently, our inquiry must look not merely to the personalities of the managers but primarily to the factors underlying the existence and continuation of the management.

And in *Hartford Gas Company,* 8 S. E. C. 758, 766,[19] the same thought is expressed:

> To satisfy condition (iii) the applicant must show that nothing in the course of relationships between the specified holding company and itself would suffice to make its management or policies "*subject to* a controlling influence, directly or indirectly, by such holding company (either alone or pursuant to an arrangement or understanding with one or more other persons) so as to make it necessary or appropriate in the public interest or for the protection of investors or consumers that the applicant be subject to the obligations, duties, and liabilities imposed" in the Act "upon subsidiary companies of holding companies." The phrase "*subject to,*" which we have emphasized, clearly does not imply continuous exertion of controlling influence by the holding company over the operating company. Thus we have pointed out that even where there is complete inaction on the part of the holding company, that fact, in

[19] Affirmed, *Hartford Gas Co.* v. *Securities and Exchange Commission,* 129 F. (2d) 794 (C. C. A. 2).

itself, "does not necessarily negate the existence of control or controlling influences". *The Detroit Edison Company,* 7 S. E. C. 968, 969 (1940).

As noted, this view was affirmed, in the *Detroit Edison* and *Hartford Gas* cases, by the circuit courts of appeals for the sixth and second circuits, respectively. These circuits are not alone; they are joined by the third circuit (*Public Service Corporation of New Jersey* v. *Securities and Exchange Commission,* 129 F. (2d) 899, certiorari denied, 317 U. S. 691), and by the court of appeals for the District of Columbia (*American Gas & Electric Co.* v. *Securities and Exchange Commission,* 134 F. (2d) 633, certiorari denied, 319 U. S. 763; *Koppers United Co.* v. *Securities and Exchange Commission,* 138 F. (2d) 577). The courts have uniformly sustained the Commission's understanding of the law.

Underlying these interpretations which assimilate latent power to the statutory standard of "controlling influence" is the realization of the practical consequence of latent power upon the behavior of those who may be aware of it. It is a matter of common experience in corporate affairs that power to control corporate action is seldom put to the ultimate test of a proxy fight, but is manifested through practical arrangements which reflect an appraisal of the possible outcome of a contest for control. Thus the daily policies

and management of a company are ordinarily shaped by an awareness of and consideration for the interests of a substantial stockholder who is in a position to contest for exclusive control with a reasonable prospect of success. For this very reason, a realistic application of the standard of "controlling influence" frequently presents troublesome fact questions, necessitating, as in this case, most thorough exploration of the historical relationships and interconnections between the companies in question, and between their respective officials, as a background for appraisal of the currently significant influences potentially affecting their conduct. The Commission has been acutely conscious of the congressional expectation that the phrase "controlling influence" would provide sufficient flexibility "to meet the varied and subtle forms which corporate interrelationships have in the past and will in the future take." See S. Rep. No. 621, 74th Cong., 1st Sess., p. 23; H. Rep. No. 1318, 74th Cong., 1st Sess., p. 9.[20] The Commission has so interpreted and applied the phrase, and its inter-

[20] The quotation in the text from the Senate and House reports rebuts the implications which the petitioner seeks (Br., pp. 27–31) to draw from Senator Wheeler's statements in the course of the legislative debate, and from the Commission's brief in this Court in *Electric Bond & Share Co.* v. *Securities and Exchange Commission*, 303 U. S. 419. Viewed in their context, these are generalized statements, merely describing the broad outlines of the Act's coverage, and making no effort to deal with particular problems of application.

pretation, as that of the agency charged with the administration of the Act, is entitled to great weight. *Gray* v. *Powell*, 314 U. S. 402, 412.

Moreover, apart from the weight to be accorded to the Commission's views, the courts which have considered the section have expressed on their own behalf similar appreciation of the need for flexibility of approach. Judge Rutledge pointed out in *American Gas & Electric Co.* v. *Securities and Exchange Commission*, 134 F. (2d) 633, at 641–2 (App. D. C.), certiorari denied, 319 U. S. 763:

> As "control" may take many different forms, so may "controlling influence," and the statute is intended to cover any form or device, which may be "pursuant to an arrangement or understanding with one or more other persons." In clause (iii) Congress has enacted an extensible formula that can be applied to "meet the varied and subtle forms which corporate interrelationships have in the past and will in the future take." It is intended to provide a broad sphere for the Commission's determinations in order to carry out the policies of the Act as expressed in Section 1. [Footnotes omitted.]

The same thought is expressed in greater detail by Judge Hamilton in *Detroit Edison Co.* v. *Securities and Exchange Commission*, 119 F. (2d) 730 (C. C. A. 6), at 738–9:[n]

[n] Certiorari denied, 314 U. S. 618.

The present Act undertakes to bring within its ambit all subsidiaries subject to "controlling influence" of a parent. This phrase should be construed in the light of the purpose of the Act of which it is a part, and when understood in this setting and in the light of its ordinary signification, it means the act or process, or power of producing an effect which may be without apparent force or direct authority and is effective in checking or directing action, or exercising restraint or preventing free action. The phrase as here used, does not necessarily mean that those exercising controlling influence must be able to carry their point. A controlling influence may be effective without accomplishing its purpose fully.

Corporate wealth has become so widely distributed that control over it has tended to become more and more remote from ownership. Ownership of corporate shares without appreciable corporate control and control of corporate wealth without appreciable ownership has become a natural phenomenon of our economic system. Seven major types of corporate control were extant when the present Act was passed and others may develop from the urge of individuals to avoid public regulation. Congress recognized this condition, and the present Act imposes a wide discretion in the Commission in determining what is "controlling influence" of a parent over a subsidiary public utility. However, this part of the present Act has its guide

post, which prevents the Commission from exercising arbitrary power in enforcing it.

The types of control referred to are: (1) through complete ownership of capital stock, (2) a majority ownership, (3) through a legal device without majority ownership, such as pyramiding through holding companies or a large issue of non-voting stock with a comparatively small issue of stock with voting rights, or voting trusts, (4) minority control, which exists when comparatively few shares of corporate stock are in the hands of one group and the remainder widely scattered, (5) management control, which exists where all the stock is so widely distributed that no stockholder takes sufficient interest in the affairs of the corporation to influence or control it, (6) proxy control through committees, (7) through interlocking corporate officers or directors.

The evidence in the case at bar shows marked features and significant incidences of the latent power of the North American Company to exercise a controlling influence over the petitioner. Compare *Natural Gas Pipeline Company* v. *Slattery*, 302 U. S. 300, 307, 58 S. Ct. 199, 82 L. Ed. 276; *United States* v. *Union Pacific Railroad*, 226 U. S. 61, 96, 33 S. Ct. 53, 57 L. Ed. 124; *Southern Pacific Company* v. *Bogert*, 250 U. S. 483, 492, 39 S. Ct. 533, 63 L. Ed. 1099; *Hyams* v. *Calumet & Hecla Mining Company*, 6 Cir., 221 F. 529; *Moulton* v. *Field*, 179 F. 673; *Rochester Telephone Corpora-*

tion v. *United States and Federal Communications Commission*, 307 U. S. 125, 145, 59 S. Ct. 754, 83 L. Ed. 1147.

These views of the Commission and the courts do not exscind the word "controlling" from the operative significance of the phrase "controlling influence." Rather they give meaning to it, as a potent instrument for discovering, not "purely hypothetical future machinations" (Pet. Br., p. 39), but the realities of present power to control—whenever the interests of the dominant entity may dictate an effort to place that power in operation.

The petitioner stresses (Br., pp. 41, 42) the failure of the Commission to find as a fact that it "is presently subject to the controlling influence of North American." The Commission concededly made no such finding; but there was no reason why it should. The Commission found, expressly, "that North American has the power—if the occasion arises and if it so desires—to make its influence felt in a substantial and affirmative manner" (R. VI, 1922–1923).[22] Whether or not the influence thus found to exist was sufficient to be "controlling" is immaterial, so long as the Commission could on the basis of its finding ra-

[22] The Commission found it unnecessary to rely upon present exertion of influence, as to which, however, it said (R. VI, 1922):

> "There is evidence to justify a finding that even at the present time North American exerts a real influence in the affairs of PG&E, even though this influence is exerted in a negative way."

tionally reach its ultimate conclusion that the petitioner had failed to establish the absence of any existing "controlling influence" by North American over its management and policies. This ultimate conclusion which the Commission reached can be upset only if the Court can decide that the evidence so strongly demanded an affirmative finding of lack of controlling influence as to exclude any "rational basis" for the Commission's refusal to make such an affirmative finding. Unless the Court can so decide, the Commission's determination must stand (*Rochester Telephone Corp.* v. *United States,* 307 U. S. 125, 146); but in any event the question is one of fact, not of law.

2. *The Burden of Proof*

The petitioner does not question that it was required to establish that it was entitled to an affirmative finding by the Commission that it was not "subject to a controlling influence" by North American. But while the petitioner may be correct in emphasizing the difficulty of proving a negative, it goes far beyond the record here in its charge that the Commission imposed upon it a burden not merely difficult, but impossible. The Commission has not even demanded such a showing as has been sanctioned by the courts[22]; it has required no

[22] The courts, treating the matter in the context of a review proceeding, have held that the burden is a heavy one: "Subdivision (iii) calls for a showing of extreme negation. Its requirement is no less than that of preponderating

more than proof by a fair preponderance of the evidence that the condition prescribed by the Act has been met. It is the petitioner, not the Commission, which would attach to the Commission's use of the word "demonstrate" a requirement of proof "which excludes possibility of error" (Pet. Br., pp. 35–38). So far as the Commission is concerned, the word "demonstrate" has been used, in this as in other cases, interchangeably with such other words, in common usage synonymous, as "prove," "show," "establish," and "meet." A similar complaint drew the particular attention of the Circuit Court of Appeals for the Third Circuit in *Public Service Corporation of New Jersey* v. *Securities and Exchange Commission*, 129 F. (2d) 899, certiorari denied, 317 U. S. 691, and was answered thus (p. 902):

> Thus, upon examination of the Commission's fact findings and opinion we discover that in arriving at its conclusion the Commission did not rest its decision upon any

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proof * * *." *Hartford Gas Co.* v. *Securities and Exchange Commission*, 129 F. (2d) 794, 796 (C. C. A. 2). The petitioner comes before the Commission as a company falling squarely within the definition of a "subsidiary company" of a holding company, by virtue of North American's holdings of more than 10% of its outstanding voting securities; if it is to succeed in its demand for an order excluding it from the definition, it must do so by presenting evidence "of such a compelling character as to have required the Commission to find" the absence of a "controlling influence". *American Gas & Electric Co.* v. *Securities and Exchange Commission*, 134 F. (2d) 633, 640–641 (App. D. C.), certiorari denied, 319 U. S. 763.

> presumption arising from the ownership of 10% of voting stock of a utility company by a holding company but relied entirely upon evidence presented at the hearing before its trial examiner as to the effect of the stock ownership upon the relations of the three corporations. Again, although the Commission used the word "demonstrated" when referring to the burden which the Act places upon the applicant, there is no basis for concluding that the word was intended to connote "absolute certainty" as Public Service would have us find. Indeed, the only conclusion which can fairly be drawn from the Commission's opinion as a whole is that it proceeded upon the theory that the burden of proof which is imposed by the Act upon an applicant is to establish by a preponderance of the evidence that it is not controlled or subject to a controlling influence by a holding company. Such a conception of the burden of proof is entirely correct in the light of the express provisions of the Act, of ordinary rules of statutory construction and of generally accepted rules of evidence.

It is the petitioner too (Br., pp. 32–34), rather than the Commission, which would rest the Commission's holding upon a conclusive inference arising from North American's stockholdings. The Commission drew no such conclusive inference; it weighed the fact of stockholdings, as it weighed all other relevant facts. It properly gave much

weight, as evidence, to the fact that North American held by far the largest block of securities in P. G. & E., amounting to 32.89% of the common stock and 17.71% of the voting power, and that the next largest holder owned less than 2% of the voting securities, the balance being widely scattered.[24] Such consideration of not only the size of North American's holdings but also the relative size and distribution of other holdings of petitioner's stock, in the light of the historical facts of North American's position and influence as a stockholder, erects no irrebuttable presumption from the fact of 10% stock ownership.

In short, as with the petitioner's contentions regarding the meaning of "controlling influence",

[24] The power of a concentrated holding in the face of a management supported only by scattered interests is graphically illustrated by the history of The Detroit Edison Company since the events set forth in the Commission and court decisions cited, *supra*, pp. 35, 39. The Commission had held that Detroit Edison was a subsidiary of North American but was not a subsidiary of American Light and Traction Company, which, although holding 20.27% of its voting stock, had been unable to secure representation on the Board over the opposition of North American. Thereafter, North American's holdings of 19.28% in Detroit Edison were reduced to less than 1/10 of 1%, leaving Light and Traction as the dominant stockholder of that company, with the next largest holdings 4.2%, 2.3% and 1.2%. Light and Traction then designated two nominees for the Board of Directors of Detroit Edison, who were elected. Detroit Edison thereupon agreed that it was a subsidiary of Light and Traction, and withdrew its application to be declared not such a subsidiary, which application had been granted during the period when North American held its concentrated block.

we believe that its contentions as to the burden of proof are in reality no more than argumentative assertions of its ultimate contention that the Commission could not rationally draw the inferences which it did from the record. Succinctly stated, the premise of petitioner's case seems to be that if it could not meet the Commission's standards, no company could. That this premise is unsound is shown by the numerous cases in which the Commission has found the burden of proof to have been successfully carried.[25] The real question in the case is not the propriety of the Commission's standards, but the propriety of the inferences which it drew from the record. To that question—the factual aspect of the case—we now turn.

II

THE COMMISSION'S DETERMINATION WAS WARRANTED BY THE RECORD

Petitioner argues that the Commission's findings are not supported by substantial evidence. This argument does not go to the material evidentiary or basic facts; petitioner has not disputed any of the Commission's findings set forth in the statement above, at pp. 8–24. The controversy

[25] The cases prior to the Commission's decision in the instant case are collected in footnote 27 to the Commission's opinion, R. VI, 1928–9. The stockholdings involved ranged as high as 42% (*Panhandle Eastern Pipe Line Company*, 9 S. E. C. 370 (1941)).

rather revolves around the conclusions and inferences drawn by the Commission from the undisputed facts, and around the Commission's refusal to draw conclusions and inferences pressed by the petitioner. Such a controversy is to be judicially examined in the light of the rules generally applied under statutes which, like Section 24 (a) of the Holding Company Act, make administrative findings of fact conclusive if supported by substantial evidence. Under such a statute, even as to mixed questions of fact and law, "where the question is one of specific application of a broad statutory term in a proceeding in which the agency administering the statute must determine it initially, the reviewing court's function is limited." *National Labor Relations Board* v. *Hearst Publications,* 322 U. S. 111, 131. In such a case, the administrative agency's determination as to coverage "is to be accepted if it has 'warrant in the record' and a reasonable basis in law." *Ibid.* Nor is the administrator precluded from drawing an inference merely because the record might equally well have supported a contrary or inconsistent inference. "The possibility of drawing either of two inconsistent inferences from the evidence did not prevent the Board from drawing one of them." *National Labor Relations Board* v. *Nevada Copper Co.,* 316 U. S. 105, 106. Cf. *National Labor Relations Board* v. *Waterman Steamship Co.,* 309 U. S. 206, 226. Nor is the standard

of review any different because the basic facts may be undisputed. *United States* v. *Louisville & Nashville R. R. Co.*, 235 U. S. 314, 320; *Federal Trade Commission* v. *Pacific States Paper Trade Ass'n*, 273 U. S. 52, 63.

In this case the record established that North American's holdings of P. G. & E.'s voting securities were by far the largest, all other holdings in such securities being small and widely scattered. Merely by withholding its votes North American could have prevented the conduct of business at any meeting of P. G. & E.'s stockholders held since 1932. Its holdings are sufficient to block any substantial reorganization of the company or its security structure. North American is a giant holding company engaged in the public utility business, with an organization well versed in all matters relating to the utility industry. As to financial matters its advice was sought when needed by the responsible officials of P. G. & E. Furthermore, North American's investment in P. G. & E. represented a substantial part of North American's own portfolio and was carried on North American's books at $63,000,000. The dividends received from P. G. & E. constituted from 20% to 25% of North American's entire corporate income. Over this vital investment North American kept a close scrutiny. Representatives of North American sat on P. G. & E.'s Board of Directors, and one of its former trusted executives

became P. G. & E's president. North American secured frequent and detailed reports concerning P. G. & E.'s business, in greater detail than those received by other members of the Board of Directors or even by the Executive Committee of that Board. Throughout the period of their relationship but one inconclusive instance was adduced in which P. G. & E.'s conduct failed wholly to satisfy North American.

The petitioner's case in substance consisted merely of testimony by its officials that the results which normally flow from such consequential holdings did not in this instance exist. The Commission found the petitioner's showing insufficient, and determined that it could not make the requested finding that petitioner's management and policies were not subject to a controlling influence by North American. That there was adequate justification for the Commission's action will appear from a more detailed examination of the facts in the record.

(1) The first and most important single fact which the record established is the distribution of security holdings. North American owns 32.89% of P. G. & E.'s common stock and 17.71% of its outstanding voting securities (R. I, 74–5; *supra,* pp. 9–10). Moreover, almost half of the voting power is in the preferred stockholders, who, because of the nature of their investment interest, are in favorable times less likely than common

stockholders to take an interest in control. This circumstance makes North American holdings of a third of the common stock of even greater strategic significance than would be indicated by the percentage of the outstanding voting securities which it holds.

The next largest stockholder owns shares giving it less than one-tenth as much voting power (R. I, 75). There are only four holdings of as much as 100,000 shares, compared with the more than 2,000,000 shares held by North American. The remainder of the stock is widely distributed in small units, among more than 95,000 stockholders (R. I, 74–75; VI, 1897–8; Pet. Ex. 20, 21 and 29; *supra*, p. 10). All the local directors together own less than 100,000 shares. There is no stockholder or present coalition of stockholders which in any way approaches North American's holdings. From ownership such as North American's, controlling influence usually follows. In the words of Judge Learned Hand, concurring, in *Morgan Stanley & Co.* v. *Securities and Exchange Commission*, 126 F. (2d) 325, 333 (C. C. A. 2), "quite aside from any implications from the statutory definition of 'subsidiary', § 2 (a) (8), I think we can take judicial notice of the fact that the ownership of twenty per cent of the voting power of a company makes the owner 'liable' to have practical control."

To offset these concentrated holdings petitioner relies only on the contention that the combined holdings of the local directors, their families, and the institutions which they represent, amount to some 800,000 shares, and upon the further possibility of rallying to their support the scattered holdings of over 58,000 shareholders residing in the territory (Br., pp. 62, 82). If they were successful in obtaining proxies from 100% of the California holders, they would still control less than 50% of the total voting securities (R. VI, 1898). Moreover, as the Commission pointed out, there is no basis in fact for assuming that there would be no cleavage among the local directors, or that issues would necessarily be sharply drawn between North American and a compact local group.[28] As businessmen having important local business interests, the local directors cannot be insensitive to the enormous amount of business patronage available to an $800,000,000 enterprise like P. G. & E. Rivalries as to the distribution of such patronage may be expected to have their effect upon the unanimity of local directors. An instance in the record where a difference of opinion did develop among the local directors as to distribution of business patronage related to the selection of a leading underwriter in connec-

[28] See R. VI, 1924, n. 24. "We think that applicant's assumption that the local management would constitute a unanimous bloc on the same side of any conflict is of doubtful validity."

tion with financing by petitioner. This incident is summarized in the Commission's opinion (R. VI, 1905–1907).[27] The very fact that North American and its representatives do not appear to have any interest in the distribution of petitioner's local business patronage would tend to strengthen its position should it display any interest in the allocation of such of petitioner's business as could not be handled by California firms.[28]

(2) The persons who were directors of P. G. & E. prior to North American's acquisition of its interest in the company understood the

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[27] Hockenbeamer desired, in part for reasons of personal friendship, to place the business with Lazard Freres, while several of the other local directors favored Blyth & Co., and in that connection it appeared that Chickering, one of the P. G. & E. directors, had been counsel for Blyth & Co. for some twenty-five years (R. II, 801; III, 1398) and that C. O. G. Miller, another director, had a son-in-law who was a partner of Blyth & Co., as well as two very close friends who were also partners there (R. II, 647, 653–4). The entire story of this jockeying for position as leading underwriter appears most revealingly in the testimony of Charles R. Blyth (R. III, 1381–1411), C. O. G. Miller (R. II, 643–660), and Black (R. III, 1091–8, 1240–91). This difference between the local directors of P. G. & E. was one in which Black, while still with North American, participated. Black at that time expressed a sympathy for Blyth & Co.'s claims, and when he later became president awarded the leading position to them. And during the period while the question of allocation of petitioner's underwriting business was under consideration, the interested bankers felt it worth while to press their claims upon North American's officials, including Black, Fogarty and Williams (R. III, 1391–1400).

[28] For the bearing of such dispute upon the public policy of the Act, see p. 73, *infra*.

power which North American's acquisition would give it. They were apprehensive as to the extent of the influence North American would wield in their company by reason of its concentrated holdings (R. II, 735, 778–9; *supra*, pp. 11–14). They asked that North American agree in advance not to use its influence to dominate or interfere with the management of the company. They wanted a written assurance and an irrevocable proxy from North American (R. II, 620–1, 735, 778–9). However, North American refused, and the old P. G. & E. management had to be satisfied with an informal agreement without any time limit (Pet. Ex. 43A; R. I, 226–7, 257–9; II, 620–1, 735–6, 778–9, 831–2; III, 1059–1062, 1123, 1127–1130). North American's attitude was that so long as P. G. & E. was operating satisfactorily "the situation did not seem to require any more attention," but that should it develop that the management was acting improperly or incompetently, it would intervene (R. IV, 1545–8). A possibility so real and vital to directors of P. G. & E. at the time North American came into the picture was hardly evidence to be disregarded by the Commission.

(3) So long as North American is satisfied with the present management, North American's voting power and the proxy machinery in the hands of the management make it virtually impossible for any other interest or group of interests to elect a majority of the directors (R. VI, 1924).

(4) Since 1932 (until April 9, 1940), North American's votes have represented 27% to 30% of the total votes cast at stockholders' meetings and, by virtue of its stockholdings, North American had the power to break a quorum at all of the stockholders' meetings during that period (R. VI, 1898–9, 1924–5; *supra*, pp. 22–23). If it had chosen to do so, no business could have been transacted at such meetings (R. VI, 1924). That "a quorum could have probably been obtained (without the representation of North American) by sending out an additional notice" (Pet. Br., p. 62) is possible, but scarcely conclusive.

(5) The ownership of virtually one-third of petitioner's common stock gives North American an effective veto power over vitally important organic forms of corporate action."[29] For instance, the Board of Directors cannot be reduced to less than five without the consent of the holders of more than 80% of the voting shares; a merger or consolidation must be approved by the holders of not less than two-thirds of each class of stock; the voting rights of any class of stock cannot be diminished without the consent of the holders of two-thirds of the shares of that class; the dividend rate or redemption price or priority on liquidation, etc., of the preferred cannot be increased without the consent of the holders of a majority of the common shares.

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[29] See Deering's Civil Code of California (1937), Div. I, Pt. IV, Tit. I, Ch. XIII.

(6) Against the background of the other facts we have discussed, the Commission found to be of material significance the fact that North American has been given the "right" to three representatives on petitioner's Board of Directors and one representative on its Executive Committee (R. VI, 1925).[30] None of P. G. & E.'s other large stockholders is represented on its Board (R. VI, 1901).[31]

(7) The Commission also regarded as significant the fact that frequent and detailed reports of every phase of petitioner's operations were sent

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[30] Fogarty's testimony in this respect is highly illuminating. He testified (R. IV, 1562–3; VI, 1925–6):

> Q. If your holdings were considerably smaller, it is very possible that you would not be entitled to two members or three representatives on the applicant's Board. You might not even have any representation on the applicant's Board, that is true, is it not?
>
> A. Yes, that is true.
>
> Q. Then, in that sense, at any rate, you would not be in a position to exercise the controlling influence over applicant's affairs that you can exercise in view of the fact that you have very large holdings.
>
> A. The difference is that the officer of the North American Company being a director of the Pacific Gas & Electric Company has a voice in its affairs as a director, whereas a small stockholder, not being a director, would not be in that position, and naturally the affairs of the company being managed by the Board and two officers of the North American Company being directors and participating in that capacity as directors, are in a different position from a small stockholder who is not a director.

[31] See note 11, *supra*.

by P. G. & E. to North American. No such reports are sent to any other stockholder. (R. VI, 1925–6; *supra*, pp. 17–19).

(8) Ever since Black became petitioner's president he has called Fogarty, chairman of North American's executive and finance committees, a number of times each year to seek advice concerning petitioner's financial affairs, and Hockenbeamer, when president of P. G. & E., had frequently sought advice of Black, who was then vice president of North American (*supra*, pp. 19–20). As Judge Rutledge said in the *American Gas & Electric Company case* (134 F. (2d) at 642): "Under some circumstances 'controlling influence may spring as readily from advice constantly sought as from command arbitrarily imposed.' Manchester Gas Co., 1940, 7 S. E. C. 57, 62."

(9) North American's latent power over P. G. & E. is also evidenced by the situation with respect to Black. The petitioner complains that the Commission over-emphasizes Black, referring to him by name in its opinion more than 60 times (Pet. Br., pp. 92–93, note). But, as the Commission stated in its opinion (R. VI, 1926–7), it could not—

> disregard the fact that applicant's most important executive officer, Black, its president, was, for eight years just prior to his appointment, a senior executive of North American. From February 1927 to June 1930 Black's primary duty as vice presi-

dent of North American was to exercise holding company supervision over the activities of the subsidiaries of Western Power Corporation. He conducted the negotiations for North American in which Western Power was transferred to PG&E and as a result of which North American acquired its interest in PG&E. For five years, from 1930 to 1935, Black was the individual in the North American organization who, more than any other one person, kept advised as to applicant's business and followed applicant's affairs in the light of North American's interest. It is also significant that since Black became president of PG&E, no effort has been made by North American to have representation on the executive committee, and no one in North American's management has followed applicant's affairs as closely as he did. It is wholly unreal to suppose that Black would be uninfluenced by these circumstances and, in his dealings with North American, would treat it as merely a large stockholder of PG&E.

(10) The Commission also attached significance to the fact that, although the record in this case covers the entire history of the relationship of P. G. & E. and North American, the only evidence offered by petitioner to show an affirmative conflict between it and North American was the testimony to the effect that P. G. & E.'s Board failed to comply with a request by North Ameri-

can's president and by Black to reconsider the dividend reduction in 1933. The request was mild in terms, and when it was refused North American did not regard the matter as of sufficient importance to call for any further attempt to obtain reconsideration."[21]

(11) Petitioner urged and the Commission found (R. VI, 1920) that the record reveals no instance in which North American has affirmatively interfered with or directed petitioner's management or policies. But the record clearly sustains the Commission's conclusion that this lack of interference was not due to an inability to influence petitioner's policies, but rather to North American's complete satisfaction with the manner in which petitioner's affairs were being conducted (R. IV, 1545–8, 1642–3; *supra,* p. 24).

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[21] C. O. G. Miller, a member of petitioner's Executive Committee and one of its most influential local directors, shared North American's view that the dividend should not have been reduced, but testified (R. II, 640):

> "After the dividend had been reduced I think I made no special effort to restore it. The mistake was made, I think, in reducing it. After the dividend had been reduced, once you have done the damage, you might as well go along until everybody is satisfied."

In the fall of 1936 the old dividend was restored on the recommendation of Black, who had meanwhile become president. Black testified that the earnings justified the restoration and that North American had not requested the action. *Supra,* pp 20–21.

Thus, Freeman testified that North American's interest in P. G. & E. was best served by the latter being regarded as a California company,[33] and Fogarty testified that North American's present inactivity in the affairs of P. G. & E. is due primarily to the fact that petitioner's business has enjoyed a normal growth and has progressed in a satisfactory manner. However,

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[33] Freeman, one of the North American representatives on P. G. & E.'s Board, testified (R. IV, 1642–3):

> Q. Well, why does the North American Company deem it advisable, if such it does, to not exercise the same supervision over the affairs of the applicant as is exercised over the affairs of its subsidiaries?
>
> A. In the first place, the Pacific Gas & Electric Company has always been regarded as peculiarly a California company, and our desire has been to see them have as strong and representative a local Board as they possibly could have. It would not be practicable to induce representative men to serve on a Board of that kind if they thought their actions were going to be subject in any way to the direction or veto of a company three thousand miles away. It would affect their public relations. *It is a situation in which our interest in the company is best served by that company being regarded as a California company, under California management.*
>
> Q. Then, would you say that your failure to exercise control of the applicant, or controlling influence over its management and policies, was due entirely to a feeling on the part of the North American Company that such a control or controlling influence was not desirable, or not to the best interests of it?
>
> A. I would say that it was not desirable from the viewpoint that it would not be to our best interests as stockholders. [Emphasis supplied.]

Fogarty indicated that if conditions changed, so would North American's attitude."

"Fogarty, North American's other representative on P. G. & E.'s Board, testified (R. IV, 1545–6, 1548):

Q. Would you say that the relationship which you have stated has existed between the North American Company and the applicant in the past was due primarily to the fact that applicant's business has enjoyed a normal growth and has progressed in a satisfactory manner?

A. Yes.

Q. You would not say, would you, Mr. Fogarty, that North American would not take a more active part in the affairs of the applicant in which it has an investment representing the market value of approximately $60-odd million, if conditions changed in such a manner that earnings were materially decreased and its ability to pay dividends on its common stock seriously threatened?

A. I don't think a drop in earnings of the Pacific Gas and Electric Company, or a change in its dividends, would be warrant for taking any active part in its management. If some conditions were to develop which were the result of improper or incompetent management, it would be an entirely different situation.

* * * * *

Q. If a situation arose in the affairs of the applicant which led you to the conclusion that the applicant would be benefited by the North American Company exerting a controlling influence over its affairs, would you take such steps as in your opinion were necessary to result in the exercise of such controlling influence?

A. Well, we would submit those views to the management and directors, and whether or not any action that would be based on those views would be taken would depend entirely upon the acquiescence and support of the management and directors of the company.

Q. But if the managers and directors of the company differed—if there arose a sharp difference of opinion between you and the management and directors on a par-

Apart from the fact that it was in the interest of good "public relations" (R. IV, 1642; VI, 1922) for petitioner to be regarded as a local company, it should be noted that the whole period since November of 1935, when Black became president, is the period since the passage of the Public Utility Holding Company Act. Presumably neither the petitioner nor North American would deny that throughout the period they have been interested in avoiding having petitioner placed in the legal status of a subsidiary. This fact is in itself sufficient to justify a certain amount of skepticism in considering North American's studied avoidance of unnecessary participation in the formal deliberations of petitioner's management—an avoidance all the more conspicuous in light of the great importance to North American of its investment in petitioner.[35] And even regarding the non-interference without skepticism, it is of no great importance. It does not establish the absence of latent power in North American to exert a controlling influence if its interests

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ticular matter, what steps would you take to oust the management?

A. I don't know that under those circumstances we could take steps to oust the management. But whatever action we would take would depend upon the circumstances that gave rise to that. It is extremely difficult to answer such a hypothetical question.

[35] As noted above (p. 9), North American's investment is carried on its books at approximately $63,000,000, and the dividend income therefrom represents from 20% to 25% of its entire corporate income.

should so dictate. It shows no more than that while affairs have been progressing favorably North American has been and still is willing to support petitioner's local management, part of which it had itself trained.

(12) What happened at the time when P. G. & E. acquired North American's subsidiaries and North American in return obtained its interest in P. G. & E. is a story commonplace in corporate history—an amalgamation of two corporations each with its own controlling group. One of the directors of the company referred to the arrangement as a marriage (R. II, 626–627). The marriage in this case was between a management-controlled company (the old P. G. & E.) and a stockholder-controlled company (the subsidiaries of North American). In such cases there are two powerful influences in the amalgamated enterprise: (1) the management group which has control of the proxy machinery, and (2) the new group which has substantial stockholdings. Sometimes there are conflicts between the two groups and one or the other triumphs.

More frequently there is no conflict, but agreement, between the two groups. An arrangement is arrived at, usually before the amalgamation is consummated, under which each party understands and respects the powers and influence of the other, as well as its own. These arrangements are gen-

erally of indefinite duration, alterable whenever either group feels that a changed equilibrium of forces (including greater or less willingness on one side or the other to enter into a contest for exclusive control) entitles it to a greater degree of influence. Until that happens, control is in effect jointly exercised, by agreement between the two influential groups, to the exclusion of the vast body of security holders.

This is precisely the situation in the P. G. & E. case. The management, in so far as it may be regarded as a group separate from North American, has control of the proxy machinery and presumably could attract substantial support from local security holders in California who represent only a little less than a majority of the voting security holders in the company. North American, with its concentrated security holdings and its vast prestige, efficient organization, and powerful financial connections, likewise is in a position to attract a substantial group of security holders and perhaps to wrest exclusive control. However, it is idle to speculate whether in a contest one group or the other would emerge victorious. It is sufficient that North American would be a formidable opponent with a substantial likelihood of success in any such contest.[36] This fact alone is an indi-

[36] If a proxy contest ever developed, North American would have a tremendous head start because of its holdings of 2,059,670 shares, with no other person owning more than 200,420. The local directors, if they banded together, own only 78,024

cation of the power of North American and an explanation of why it is to the advantage of the management of P. G. & E. to permit North American to share in the control of the company without putting it to the ultimate test.

This arrangement as to the relative positions of North American and the local directors has worked well for both parties. To the local interests in the management the arrangement has given security. They have been permitted to run the business assured that so long as North American is satisfied it is virtually impossible for any other interest or interests to remove them from the Board of Directors. On the other hand, the local management knows that North American keeps a close scrutiny over every phase of its business and

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shares; even if they could each vote all stock which they represent as fiduciaries or otherwise, they would start the contest with less than 800,000 shares.

Since the preferred stockholders of P. G. & E. have had an uninterrupted record of receiving their fixed preferential dividends, which are currently being earned by a substantial margin, they are far less likely than common stockholders to evidence an interest in managerial problems. For that reason the concentration of North American's holdings in the common stock and its 32.89% interest in that stock are particularly significant in considering a possible contest over control. In appealing for the support of fellow stockholders North American would have the advantage of being able to point to many years of experience in the public utility field, to the close study given by its officers to petitioner's affairs, and also to its own tremendous stake in the earnings of petitioner.

that North American is in a position, by reason of its stockholdings, to veto any special action requiring the vote of two-thirds of the outstanding stock. Since the inception of the arrangement P. G. & E. could have conducted no business at any of its stockholders' meetings without the approval and votes of North American.

This background provides to the local management of P. G. & E. every incentive to insure that its actions shall be satisfactory to North American and shall not displease that company. Not only is its every transaction of any significance revealed in reports to North American and its directors, but the advice of the North American representatives has been frequently sought, at least on financial matters, originally by Hockenbeamer, president of the company, and later by his successor, Black, himself a North American man appointed to the presidency of P. G. & E. as a result of his contact with the directors of that company as the representative of North American in charge of P. G. & E. matters.

So satisfactory has been the response of the directors of P. G. & E. to the realities of the situation that North American has had no occasion to exercise overtly any of its powers over the management.

The Commission deals with the question of control not only under the Public Utility Holding Company Act but also under the other statutes

which it administers."[27] The analysis made above is one which accords with the ordinary experience of the Commission in its dealing under these various statutes. The petitioner, as we have seen, has brought no evidence not thoroughly consistent with the picture thus presented. In the face of the insubstantial character of the opposing testimony, it seems plain that the Commission was entitled to analyze the situation as it did, and that it did not act without rational basis when it refused to believe that the facts in the record established that P. G. & E. was not subject to a controlling influence by North American.

(13) The final question before the Commission was whether the petitioner had shown that, even if its management or policies are subject to a controlling influence by North American, nevertheless it is not "necessary or appropriate in the public interest or for the protection of investors or consumers" that it be subject to the obligations, duties, and liabilities imposed by the Act on subsidiary companies of holding companies. In

[27] For instance, the existence or non-existence of a control relationship is often involved in determining whether registration is required under the Securities Act of 1933; in deciding whether adequate disclosure has been made in registration statements under that Act and in applications for registration, annual reports and proxy solicitations under the Securities Exchange Act of 1934; in qualification of indenture trustees under the Trust Indenture Act of 1939; and in the administration of numerous regulatory provisions of the Investment Company Act of 1940.

reaching the conclusion that petitioner had not sustained its burden of proof in this respect, the Commission used as a guide the views of the court in *Detroit Edison Co.* v. *Securities and Exchange Commission,* 119 F. (2d) 730, 739–740 (C. C. A. 6), where the court, in discussing the significance of the quoted phrase in Section 2 (a) (8), said:

> The phrase "public interest" as used means that the public has some pecuniary interest or an interest by which legal rights or liabilities of its individual members are affected by the operation of the utility. The phrase is not to be construed as requiring the Commission to find that the conduct of the applicant's business has or will affect the public adversely. The statute contemplates action prospectively. It is a preventive measure intended to regulate action before the interests of those concerned are adversely affected. The prime factors in determining statutory exemption are the size and extent of the company involved, the inter-company relationship, the distribution of its securities and the opportunity presented because of the relationship between the parent and subsidiary for excessive charges for services, construction work, equipment and materials, and the transactions entered into in which evil may result, because of the absence of arms' length bargaining or restraint of free and independent competition.

The Commission adverted to the undisputed facts that petitioner "is a company with stated assets of almost $800,000,000, serving in excess of 1,500,000 customers; its securities are listed and traded on national securities exchanges and are owned by investors throughout the country" (R. VI, 1929). The size of the petitioner, the large number of its customers and the nationwide trading in and distribution of its securities obviously make applicable the finding of Congress in Section 1 (a) of the Act that public utility holding companies and their subsidiary companies are affected with a "national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States." These facts likewise make applicable to petitioner the finding of Congress, in Section 1 (b) of the Act, that "the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers" are or may be adversely affected when certain enumerated conditions exist.

We do not contend that the record justified a finding that the more spectacular of the evils enumerated have actually existed in the relationship of petitioner and North American. The Commission emphasized in its opinion (R. VI,

1930) that its decision should not be taken to indicate "that the influence of North American necessarily is or will be improperly exercised." But the Act speaks not only of evils actually existing, but of interests of investors which "are or may be" adversely affected. Section 1 (c) declares it to be the policy of the Act to "eliminate the evils" enumerated in Section 1. In short, the Act is preventive, not punitive, in nature.

Moreover, in view of the size of petitioner, the existence of the relationship of holding company and subsidiary between it and North American in itself exemplifies a concentration of control which is one of the major evils found to exist, namely, "when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties" (Section 1 (b) (4)). The Report of the National Power Policy Committee on Public-Utility Holding Companies (S. Rep. No. 621, 74th Cong., 1st Sess. (May 13, 1935), Appendix) stresses the evils of unnecessarily expanded monopoly resulting from the "concentration of control in the electric and gas industries through the device of the holding company" which it found "has assumed tremendous proportions." As to this the Report states:

> "Numerous studies have already shown, and the report of the Federal Trade Commission further demonstrates, that the con-

centration of control in the electric and gas industries through the device of the holding company has assumed tremendous proportions. While the distribution of gas or electricity in any given community is tolerated as a "natural Monopoly" to avoid local duplication of plants, there is no justification for an extension of that idea of local monopoly to embrace the common control, by a few powerful interests, of utility plants scattered over many States and totally unconnected in operation. Such intensification of economic power beyond the point of proved economies not only is susceptible of grave abuse but is a form of private socialism inimical to the functioning of democratic institutions and the welfare of a free people.[28]

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[28] Similar thoughts were expressed by the President in his message of March 12, 1935, transmitting to the Congress the Report of the National Power Policy Committee:

> In its destruction of local control and its substitution of absentee management, it has built up in the public-utility field what has justly been called a system of private socialism which is inimical to the welfare of a free people.
>
> Most of us agree that we should take the control and the benefits of the essentially local operating utility industry out of a few financial centers and give back that control and those benefits to the localities which produce the business and create the wealth. We can properly favor economically independent business, which stands on its own feet and diffuses power and responsibility among the many, and frowns upon those holding companies which, through interlocking directorates and

Under the regulatory provisions of the Act this problem is dealt with, *inter alia,* by the provisions which authorize the Commission to impose conditions in connection with security issues of subsidiary companies (Section 6 (b)) and to require the "maintenance of competitive conditions" in many types of transactions (Sections 12 (d), 12 (f), 12 (g), 13 (c), 13 (e) and 13 (f)). The principal exercise of such regulatory jurisdiction by the Commission has been under its rule (U–50; 17 C. F. R., 1941 Supp., 250.50) requiring competitive bidding for security issues. Indeed, if we accept petitioner's protestations that there are unlikely to be any transactions on its part which might contravene other regulatory provisions of the Act, then the one important consequence of subjecting petitioner to the obligations of a subsidiary company would be to render its

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other devices, have given tyrannical power and exclusive opportunity to a favored few. It is time to make an effort to reverse that process of the concentration of power which has made most American citizens, once traditionally independent owners of their own businesses, helplessly dependent for their daily bread upon the favor of a very few, who, by devices such as holding companies, have taken for themselves unwarranted economic power. I am against private socialism of concentrated private power as thoroughly as I am against governmental socialism. The one is equally as dangerous as the other; and destruction of private socialism is utterly essential to avoid governmental socialism.

future issues subject to the requirement of competitive bidding.[39]

When the Commission has been unable to find that the management and policies of one company are not subject to the controlling influence of another holding more than 10% of its stock, and where the companies involved are of such size that their financing and other transactions in interstate commerce may affect the national economy in the manner recited in the Act, it becomes a question primarily for administrative determination whether it is in the public interest to subject the subsidiary company to regulation under the Act. In this case there is no dispute as to the factual importance of petitioner's size and financing to the national economy. The only question is that of resulting public interest. The Commission's conclusion with reference thereto is clearly within its administrative competence, and neither arbitrary nor capricious, and as such, we submit, must be allowed to stand.

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[39] During the period subsequent to the Commission's order in the case petitioner has issued some $141,375,000 principal amount of securities which were registered with the Commission under the Securities Act of 1933; however, in reliance on the "stay" granted by the court below (see note 5, *supra*) these were not submitted to regulation under the Holding Company Act. The leading underwriter for such securities was in each instance Blyth & Co., the firm which had emerged as the successful contender for that position under the circumstances referred to at p. 53, *supra*.

III

THE COURT BELOW PROPERLY AFFIRMED THE COMMISSION'S ORDER UPON AN EQUAL DIVISION OF THE JUDGES PARTICIPATION IN THE DECISION

The petitioner contends that it was error for the court below to affirm the order of the Commission by an equal division (Pet. Br., pp. 97-100). Although it is not entirely clear from the petitioner's brief exactly how it would have this alleged error remedied by this Court, it appears from the petition for the writ (p. 33) that the petitioner's proposal is that the Court should remand the case to the court below for further consideration when the existing vacancy in that court shall be filled (which we understand has very recently occurred). The petitioner's position is persuasive neither as to the law involved nor as to practical considerations.

1. As we understand petitioner's argument, it is that the review proceeding in the circuit courts of appeals under Section 24 (a) of the Act is in the nature of an original determination of a justiciable controversy, which must be decided for or against the petitioner by a majority of the court. Petitioner concedes (Pet. Br., p. 100) that it is proper for an equally divided appellate court to affirm a judicial decision, but urges a distinction with regard to decisions of an administrative tribunal. To support the argument, cases are cited which either involve the entry of a judgment in the first instance (*In re First Congressional*

District Election, 295 Pa. 1, 144 Atl. 735 (1928)), or depend upon a statute which requires a majority of the judges of the court to issue any order, judgment or decree (*Deglow* v. *Kruse*, 57 Ohio St. 434, 49 N. E. 477 (1898); *In re Kings Co. Elevated R. R. Co.*, 78 N. Y. 383 (1879)). These cases are clearly irrelevant.

Under the provisions of Section 2 (a) (8) here involved—as distinguished from other types of statutes, and indeed from certain other orders of the Commission under the Holding Company Act [10]—the orders of the Commission are self-operative. The petitioner was subject to the Act as a subsidiary of North American by force of the statute itself, and could be relieved of its responsibilities as such only on a Commission finding that it was "not subject to a controlling influence" by North American. The Commission's refusal to make such a finding left the statute operative as to petitioner unless the Commission's determination should be set aside on review.[11]

"Affirmance" by the reviewing court thus has in such a case as this no greater or different effect

[10] It is unnecessary for present purposes to consider the effect of an equally divided reviewing court upon orders of the Commission under other provisions of the Act, or the possibly different problem which might be presented under such statutes as the original Federal Trade Commission Act or the National Labor Relations Act, where sanctions for the administrative order are dependent upon a judicial decree of enforcement.

[11] For proceedings with respect to the *ex parte* "stay" of the Commission's order entered by the court below, see note 5, *supra*.

than a failure to set aside or a dismissal of a petition to review.[42] In the review proceeding the burden is on the petitioner to establish his case, both because of his position as applicant for an exception under the statute and because of the weight given to an administrative determination.[43] If the judges of the reviewing court divide equally, the Commission's order cannot be set aside, for petitioner has not satisfied this burden. The situation is comparable to that of a single judge who finds the considerations in a case evenly balanced; he then decides against the party required to make an affirmative showing. Thus even if the case is not governed by the well-established rule applicable to appellate review of the decisions of a lower court, the result is necessarily the same. It should be noted that there is no indication of dissent below from the conclusion that an equal division among the judges as to the merits should result in affirmance of the Commission's order (R. V, 1776).

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[42] In *Detroit Edison Co.* v. *Securities and Exchange Commission*, 119 F. (2d) 730, 740 (C. C. A. 6), certiorari denied, 314 U. S. 618, the action of the circuit court of appeals sustaining the Commission's order took the form of merely denying the petition to review.

[43] This is true as to conclusions of law as well as findings of fact; the weight which this Court has ascribed to the former (*St. Joseph Stock Yards Co.* v. *United States*, 298 U. S. 38, 53; *United States* v. *American Trucking Associations, Inc.*, 310 U. S. 534, 549) should prevent a court from setting them aside if it thought the considerations evenly balanced.

2. If the petitioner's proposal is that this Court should as a matter of discretion remand the case to the court below for further consideration, such a proposal should, we submit, be rejected as impractical. A similar contention was made to the court below as a ground for granting a second reargument, and on consideration was rejected. The exercise of its discretion by the lower court in determining not to grant a second rehearing is clearly not subject to reexamination by this Court except for abuse of discretion. In the light of the extended period during which this case has been pending,[44] no abuse can be claimed in putting an end to further prolongation of the litigation. See the discussion in *Brown v. Aspden's Adm'rs.*, 14 How. 25, 27–28.[45]

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[44] The petition to review was filed September 18, 1941 (R. V, 1671, 1695), and the second petition for rehearing was denied on February 23, 1944 (R. V, 1777). During this period and to the present time, the petitioner has not subjected itself to regulation under the Act because of the *ex parte* "stay" granted by the court below. See note 5, *supra*.

[45] Chief Justice Taney, speaking for a unanimous Court, denied rehearing on an earlier order of affirmance entered upon an equal division of the Justices. He said in part (p. 28):

> "And if it is to be understood, that cases of this description are not to be finally decided without the concurrence of a majority of the whole bench, it would be an useless consumption of time to hear them in the absence of any one judge, because it would be uncertain whether a judgment could follow after the argument. And it is easy to foresee the inconvenience, delay, and expenses to which a practice of that kind would subject the parties, and the uncertainty and confusion it would produce (to the great injury of other suitors) in the order of business as it stands on the docket of the court."

In addition, the case is now before this Court on certiorari, all of the substantial issues raised below are now being fully presented to this Court, and it would seem entirely fitting that under these circumstances this Court should finally decide the questions at issue. To remand would result only in delay.

CONCLUSION

We respectfully submit that the refusal of the Commission to render the finding requested by the petitioner was based upon evidence and inferences which had warrant in the record and a reasonable basis in law; that the court below properly affirmed the order of the Commission; and that the judgment of that court should in turn be now affirmed.

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